

REPORT OF THE AUDITOR-GENERAL TO THE KWAZULU-NATAL PROVINCIAL LEGISLATURE AND COUNCIL ON MPOFANA MUNICIPALITY

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the financial statements of the Mpozana Municipality set out on pages ... to ..., which comprise, the statement of financial position as at 30 June 2014, the statement of financial performance, statement of changes in net assets, the cash flow statement and the statement of comparison of budget information with actual information for the year then ended, and the notes, comprising a summary of significant accounting policies and other explanatory information.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Local Government: Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2013 (Act No. 2 of 2013) (DoRA), and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-general's responsibility

3. My responsibility is to express an opinion on the financial statements based on my audit. I conducted my audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the general notice issued in terms thereof and International Standards on Auditing. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the municipality's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the municipality's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Basis for qualified opinion

Investment property

6. The municipality's records for investment property did not include sufficient information to enable the separate identification of land and buildings. As a result, I was unable to obtain sufficient appropriate audit evidence for the amount disclosed as investment property in note 2 to the financial statements and I could not confirm the investment property by alternative means. Consequently, I am unable to determine whether any adjustments relating to investment property stated at R13,92 million (2013: R5,34 million) in the financial statements were necessary. Additionally, I was unable to confirm whether any adjustments relating to the revaluation reserve stated at R8,58 million in the financial statements were necessary.

Commitments

7. The municipality did not have adequate systems to maintain records of contractual commitments for capital and operating expenditure. As a result, I was unable to obtain sufficient appropriate audit evidence for the amounts disclosed as commitments in note 40 to the financial statements and I could not confirm the disclosure by alternative means. Consequently, I was unable to determine whether any further adjustments to the capital and operating commitments stated at R15,50 million and R9,52 million respectively in the financial statements were necessary.

Payables from exchange transactions

8. The municipality did not have adequate systems to maintain records of receipts from consumer debtors. The amount disclosed as payables from exchange transactions includes an amount of R4,19 million relating to debtor payments received in advance, as disclosed in note 17 to the financial statements. I was unable to obtain sufficient appropriate audit evidence for this amount and I could not confirm this amount by alternative means. Consequently, I was unable to determine whether any further adjustment to the payables from exchange transactions stated at R8,64 million in the financial statements was necessary.

Irregular expenditure

9. The municipality made payments in contravention of the supply chain management requirements, resulting in irregular expenditure being understated by R1,49 million (2013: R20,81 million).
10. Additionally, I was unable to obtain sufficient appropriate audit evidence for irregular expenditure of R8,26 million and the condonation thereof of R251 738 relating to the year ended 30 June 2013 due to an inadequate records management system. I was unable to confirm the disclosure by alternative means. Consequently, I was unable to determine whether any further adjustment to the previous year irregular expenditure stated at R8,01 million in note 48 to the financial statements was necessary.

Unauthorised expenditure

11. The municipality did not have adequate systems to identify and correctly record unauthorised expenditure relating to the prior year. I was unable to obtain sufficient appropriate audit evidence for unauthorised expenditure of R12,06 million and the condonation thereof related

to the year ended 30 June 2013. I was unable to confirm the disclosure by alternative means. Consequently, I am unable to determine whether any further adjustment to the unauthorised expenditure comparative stated at R5,12 million as stated in note 46 to the financial statements was necessary.

Consumer debtors

12. The municipality did not have adequate systems to maintain records of receipts from consumer debtors. The amount disclosed as consumer debtors is stated net of R2,16 million relating to unallocated receipts from consumers. I was unable to obtain sufficient appropriate audit evidence for this amount and I could not confirm this amount by alternative means. Consequently, I was unable to determine whether any further adjustment to consumer debtors stated at R23,31 million as stated in note 11 to the financial statements was necessary.

Qualified opinion

13. In my opinion, except for the possible effects of the matters described in the basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of the Mpofana municipality as at 30 June 2014 and its financial performance and cash flows for the year then ended, in accordance with the SA Standards of GRAP and the requirements of the MFMA and DoRA

Emphasis of matters

14. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Material losses

15. As disclosed in note 51 to the financial statements, material losses to the amount of R 10,36 million were incurred as a result of electricity losses due to electricity line losses within the electricity network infrastructure.

Going concern

16. As disclosed in note 44 of the annual financial statements, the municipality does not have sufficient cash to support unspent grant monies. The unspent conditional grants liability amounts to R15,74 million and the municipality has investments to the value of R11,85 million.

Additional matter

17. I draw attention to the matter below. My opinion is not modified in respect of this matter.

Unaudited disclosure notes

18. In terms of section 125(2)(e) of the MFMA the municipality is required to disclose particulars of non-compliance with the MFMA. This disclosure requirement did not form part of the audit of the financial statements and accordingly I do not express an opinion thereon.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

19. In accordance with the PAA and the general notice issued in terms thereof, I report the following findings on the reported performance information against predetermined objectives for selected objectives presented in the annual performance report, non-compliance with

legislation as well as internal control. The objective of my tests was to identify reportable findings as described under each subheading but not to gather evidence to express assurance on these matters. Accordingly, I do not express an opinion or conclusion on these matters.

Predetermined objectives

20. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the following selected objectives presented in the annual performance report of the municipality for the year ended 30 June 2014:
- Objective 4: Basic Service Delivery and Infrastructure Development on pages x to x
21. I evaluated the reported performance information against the overall criteria of usefulness and reliability.
22. I evaluated the usefulness of the reported performance information to determine whether it was presented in accordance with the National Treasury's annual reporting principles and whether the reported performance was consistent with the planned objectives. We further performed tests to determine whether indicators and targets were well defined, verifiable, specific, measurable, time bound and relevant, as required by the National Treasury's *Framework for managing programme performance information* (FMPPI).
23. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
24. The material findings in respect of the selected objectives are as follows

Objective 4: Basic Service Delivery and Infrastructure Development

Usefulness of reported performance information

Basis: Consistency of targets

Reported targets not consistent with planned targets

Basis for qualified conclusion

25. Section 41(c) of the Municipal Systems Act requires the integrated development plan to form the basis for the annual report, therefore requiring consistency of objectives, indicators and targets between planning and reporting documents. A total of 43% of the reported targets were not consistent with those in the approved integrated development. Furthermore, one reported target was adjusted in the annual performance report and not in the IDP or the SDBIP. This was due to the lack of review on the alignment between planning and reporting documents.

Compliance with legislation

26. I performed procedures to obtain evidence that the municipality had complied with applicable legislation regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key legislation, as set out in the general notice issued in terms of the PAA, are as follows:

Budgets

27. Expenditure was not incurred in accordance with the approved budget in contravention of section 15 of the MFMA.

Annual financial statements, performance and annual reports

28. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the Municipal Finance Management Act. Material misstatements of non-current assets, current assets, current liabilities, expenditure and disclosure items identified by the auditors in the submitted financial statements were subsequently corrected or the supporting records were provided subsequently, but the uncorrected material misstatements and supporting records that could not be provided resulted in the financial statements receiving a qualified audit opinion.
29. Financial statements were not submitted for auditing within two months after the end of the financial year, as required by section 126(1)(a) of the MFMA.

Procurement and contract management

30. Goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations as required by SCM regulation 17(a) & (c).
31. Goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a).
32. Awards were made to providers who are in the service of other state institutions or whose directors/ principal shareholders are in the service of other state institutions, in contravention of MFMA 112(j) and SCM regulations 44. Similar awards were identified in the prior year and no effective steps were taken to prevent or combat the abuse of the SCM process in accordance with SCM regulation 38(1).
33. Contracts and quotations were awarded to bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, as required by SCM regulation 13(c).
34. Invitations for competitive bidding were not always advertised for a required minimum period of days, as required by SCM regulation 22(1) & 22(2).

Expenditure management

35. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA.
36. An effective system of expenditure control, including procedures for the approval and withdrawal of funds, was not in place, as required by section 65(2)(a) of the MFMA.
37. Reasonable steps were not taken to prevent unauthorised expenditure, irregular expenditure and fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.

Revenue management

38. An effective system of internal control for debtors and revenue was not in place, as required by section 64(2)(f) of the MFMA.

Internal control

39. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with legislation. The matters reported below under the fundamentals of internal control are limited to the significant deficiencies that resulted in the basis for qualified opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report.

Leadership

40. There was inadequate oversight on the review of annual financial statements submitted for audit, no formulation of a process to ensure consistency of reported performance information, and inadequate oversight over compliance with regulations. Vacancies in key positions in senior management had a direct impact on the municipality's ability to implement and monitor the financial and performance management systems of internal control, as well as the effectiveness of action plans to prevent the recurrence of prior year audit findings.

Financial and performance management

41. The record keeping of the municipality was inadequate to support reported information. Annual financial statement disclosures were not adequately supported by documentation. Daily controls were not adequate to support accurate financial records, reconciliations or reporting.

Governance

42. Risk assessments were not adequate for the purpose of internal audit and audit committee to ensure that prior year findings were addressed.

OTHER REPORTS

Investigations

43. Two investigations are currently being performed by municipal legal representation relating to cases detected in the current and prior periods in respect of abuse of municipal vehicles and unauthorised removal of cash from municipal premises by a director. The outcome is expected to be finalised in February 2015. Further internal investigations are being conducted that are expected to be finalised in March 2015 relating to inadequate handling of cash and misrepresentation of monies received, and the fraudulent issuing of licences and permits.

Auditor-general
Pietermaritzburg

09 December 2014



AUDITOR-GENERAL
SOUTH AFRICA

Auditing to build public confidence